UNITED STATES DEPARTMENT OF AGRICULTURE
Agricultural Marketing Service
(Dairy Programs)

Milk in the Central Marketing Area	)	
	)	**Dkt AO 313-A44**
Hearing on Proposals to Limit Pooling of Out-of-Region Milk	)	**DA 01-07**

POST-HEARING BRIEF ON BEHALF OF:
FOREMOST FARMS, LAND O'LAKES, FIRST DISTRICT ASS'N, FAMILY DAIRIES USA, MIDWEST DAIRYMEN'S COOP., MANITOWAC MILK PRODUCERS COOPERATIVE, AND MILWAUKEE COOPERTATIVE MILK PRODUCERS (HERINAFTER "THE COOPERATIVES")

This brief is submitted in opposition to the discriminatory and inefficient elements of hearing proposals 1, 3, 5, and 7 by Dairy Farmers of America and allied organizations that dominate the supply of raw producer milk to the Central Marketing Area ("DFA"). The proposals are designed to benefit DFA at the expense and disadvantage of thousands of members of the Cooperatives identified above by causing (1) disassociation from the Central Marketing Area milk pool, (2) artificial aggravation of costs to remain associated with the Central pool, or (3) reduced blend prices resulting from more of the region's surplus milk production moving to the Order 30 pool. As described below, these proposals should not even be considered without broader notice and

hearing addressing the alleged "problem" that DFA admits transcends the Central and Upper Midwest markets, and that all participants perceive will have significant implications beyond Order 32. On its merits, the proposals are contrary to decades of USDA policy and runs afoul of AMAA requirements (1) for uniform producer prices, (2) for producer pricing which is not dependent on handler use, and (3) which prohibit trade barriers. It also seeks to employ government process in a way that conflicts with Equal Protection guarantees.

In brief, the proposals are collectively and individually designed to restrict, and would in fact restrict, the ability of the Cooperatives to market milk on the Central Market. This is the unabashed explanation in testimony by DFA (Exhibits 8, 10, 11), and the unanimous conclusion in testimony of witnesses for the Cooperatives (E.g., testimony of Kurth, Hahn, Gulden, Gran, and Tonak). If successful in its objectives, the DFA proposals would cause some 400 million pounds of milk to move off the Order 32 pool on to Order 30, resulting in a decline of 15 cents per hunderweight in PPD prices paid to existing Order 30 producers and a drop of 59 cents per hundredweight for those producers who were forced to shift from an Order 32 plant to an Order 30 plant. Exhibit 17; Testimony of Kurth. Since average producer net income is in the range of $ 0.75 to $ 1.00 per hundredweight (Exhibits 18, 19; Testimony by witnesses for the Cooperatives), the proposals would have a significant and

adverse impact on the livelihood of farmers, small business enterprises, associated or newly associated with the Upper Midwest pool by reducing their income by more than 30% to 50% in many cases.[1] A correspondingly significant beneficial effect would accrue for producers remaining on the Order 32 pool – particularly those who may retain privileged pooling status without any new regulatory burdens.

This effort to create market barriers and zip code discrimination comes at a time when blend price differences between Wisconsin and Iowa, the dominant milk producing states in Orders 30 and 32, are not much different than they were before federal order reform. For Calendar years 1998 and 1999, Iowa's blend piece was 22 cents higher than the Chicago regional blend price. FMOS – 1999 Annual, Ts. 29 – 32. Since federal order reform, the Order 32 – Order 30 blend price (PPD) difference has enlarged significantly (E.g., Exhibit 17). The DFA proposals are intended to enlarge the difference even more.

Producers in the Central Market have also enjoyed, since federal order reform, a blend price (PPD) that exceeds the Class III price by a larger amount than prior to reform. The Class III to uniform price spread before federal order reform was 45 cents in 1999 (FMOS 2000, supra). In the first year of reform,

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[1] Many of those who would be directly affected by the proposals received no notice, and even the notice itself – perhaps characteristically for federal milk order hearings – did not contain a plain English explanation of the economic consequences of the esoteric words and concepts published in the proposals.
The Cooperatives renew their objection concerning the failure of the Notice of Hearing to reach and to inform those who would be adversely affected. See. Hearing Tr. pp. 124-137

this increased to $ 1.54. In the first 9 months of 2001, the Class III – uniform price spread was $ 1.16. Exhibit 5, T. 1. This is because the price of milk for cheese no longer drives other class prices. But in the Upper Midwest, Class III prices drive the blend or BFP.

ARGUMENT

The DFA proposal seeks, in effect, to shift to Upper Midwest dairy farmers alone a unique burden of Class III-dependent prices while Order 32 local producers are entitled to a disproportionate share of the benefit of the new formula for other uses of milk. This is not only in conflict with the stated administrative objectives of reform, but is also in conflict with Congressional objectives to mitigate the economic strain on Upper Midwest producers by mandating a greater Class I price increase in Option 1-A than for other areas. There are a number of additional and sound legal reasons to resist DFA's effort to turn back the clock.

Even under ordinary circumstances, standards for reasoned administrative action are "strict and demanding." *Motor Vehicle Manufacturers Association v. State Farm Mutual,* 463 U.S. 28, 48 (1983). Milk Marketing Order rulemaking standards are further constrained because the Secretary "does not have 'broad dispensing power'." *Zuber v. Allen,* 396 U.S. 168, 183 (1969). However, before we examine Legislative authority for DFA's proposed rules,

we suggest that the proposal was improvidently noticed for hearing under only one Order when its is clear from DFA's own remarks that the issue should be addressed only in an inter-market hearing so that others affected may have an opportunity to present evidence and comment on policy while the regulatory clay is still pliable.

A. THE PROCEEDING SHOULD BE TERMINATED AS TO PROPOSALS ADDRESSED TO THE ALLEGED "PROBLEM" OF DISTANT MILK ASSOCIATED WITH THE ORDER 32 POOL, AND CONSIDERED, IF AT ALL, ONLY UPON NOTICE OF A NATIONAL HEARING.

The Secretary has long exercised the reasonable policy that where milk marketing issues and proposed rules have significant impact beyond a single market or region, it is appropriate to give express notice to all handlers and producers that may be affected, and to open other orders or all orders to appropriate rulemaking amendments on the issue. Failing such notice to affected parties, the Secretary has terminated order amendment hearings where the hearing record revealed significant extra-market impact from proposals that initially appeared to be limited to markets included in the Notice of Hearing. *See,* 52 Fed. Reg. 15951 (May 1, 1987)(terminating consideration of marketwide service proposals for southeast markets because, if adopted, "inter-market milk movements throughout this broad area ...would result in producers in the [markets subject to the hearing notice] bearing the burden of balancing

milk supplies for [other markets]....". In a Texas Order proceeding, the Secretary terminated consideration of a proposal to reduce Class III prices in part because the problem addressed involved "the sale and processing of milk over a broad region that extends well beyond the Texas marketing area." 49 Fed. Reg. 20825, 20828 (May 17, 1984):

> Furthermore, consideration of the long term manufacturing efficiency issue has implications to the level of Class III pricing throughout the Federal order system and the national market for manufactured dairy products. Thus, it is preferable that the issue not be addressed on the basis of a record that is limited to ... one market."

Id., at 20830.[2]

Following the bad example of its organizational predecessors, DFA again seeks to effect a rule change on the basis of a record limited to one market, while at the same time unabashedly (and correctly) admitting that the issue it raises has implications throughout the Federal order system, as amended and reformed following the 1996 Farm Bill.

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[2] *See also* 53 Fed. Reg. 24298, 24310-11 (June 28, 1988)(Chicago Order decision), reversing a recommended decision on a pricing issue in response to a general belief that the notice of hearing was inadequate.

B. THE DFA PROPOSAL IS INCONSISTENT WITH USDA'S LONGSTANDING POLICIES.

DFA's lengthy hearing argument in support of proposals for special regulatory burdens imposed on "outside" producers and plants repeatedly invoked claims that the proposals would simply reinstitute pre-reform pooling policies. These claims take a myopic view of regulatory history.

For over a half-century, it has been USDA's policy to design plant and producer pooling provisions to provide a regulatory balance between the fluid needs of the market and transportation efficiency to meet those needs. 12 Fed. Reg. 5617, 5623 (August 21, 1947)(Chicago Order "standby plant" Decision); "Marketing efficiency is optimized when a handler can decide how and where to move milk supplies under a handler's control .... No valid purpose is served in requiring each producer's milk to be received at a pool plant eight days per month." 46 Fed. Reg. 21958 (April 14, 1981)(Idaho Decision); accord, 43 Fed. Reg. 33652, 33656 (July 31, 1978).

"Shipments should not be encouraged to a greater degree than necessary to satisfy fluid milk needs.... To do so results in uneconomic movements of milk to distributing plants solely for pooling purposes rather than to meet fluid milk needs." 43 Fed. Reg. 12695, 12699 (March 27, 1978)(New England Order Decision); 53 Fed. Reg. 24296, 24308 (June 28, 1988 (Chicago Decision modifying reserve supply plant provision and touch base requirement); 47 Fed

Reg. 44268. 44293 (October 7, 1982)(Southwest Plains producer pooling standards designed to maximize transportation efficiency). Orderly marketing is promoted by *not requiring* shipments to distributing plants when such shipments are not needed to supplement their fluid milk needs. 52 Fed. Reg. 27505, 27210-12 (July 20, 1987)(Decision, Michigan and Ohio Marketing Orders).

The need to provide a means for surplus Grade A milk to share in fluid milk revenue has been recognized by regulators, economists and courts for over six decades. *United States v. Rock Royal Coop.*, 307 U.S. 533, 550 (1939). It was to avoid the disruptive results of surplus milk competing for a fluid outlet that Congress made provision for all milk to participate in a marketwide pool. The regulatory desirability of allowing Grade A milk to participate in the pool with only minimum requirements of market association has shaped Order 30 and its predecessors. The Secretary has recognized that Grade A milk excluded from the pool, and competing for limited access to the fluid market under rigid performance rules, is a greater threat to orderly marketing in surplus marketing areas than excess or "unneeded" milk supplies sharing in marketwide proceeds.

The proposal, particularly as intended by DFA to extend well beyond the boundaries of the Central and Upper Midwest Markets, would also constrain the utility of blend price differences as a principal economic signal to producers to

choose one market over another in making milk sales, because the proposals would create far greater financial burdens to respond to those signals.

As explained by the Secretary after the previous national hearing review and reform process in 1990:

> Producers make their production and marketing adjustments on the basis of changes in blend prices and differences in blend prices among orders. It is not uncommon for supply areas of individual orders to expand or contract in response to blend price changes over time. Also, *because milk is free to move to handlers regulated under different orders, it is not uncommon for milk to shift from one order to another in response to blend price differences that result from changes in supply and demand conditions under different orders.*

59 Fed. Reg. 42422, 42426 (August 17, 1994)(emphasis supplied). In his Second Amplified Decision, the Secretary reemphasized:

> Blend price changes (and differences in blend prices among orders) provide the economic signal for producers to make production decisions and for making marketing adj stments.

61 Fed Reg. 49081, 49086 (Sept. 18, 1996). DFA's vision of the system would stop many a producer in his marketing tracks even if blend prices alone signaled a market shift would be desirable. Provisions such as proposed by DFA would make the alternative market financially impractical or simply unattainable so long as the producer elected not to affiliate with DFA or its allies.[3]

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[3] The Agricultural Fair Practices Act, 7 U.S.C. §§2301-2306, also administered by the Secretary of Agriculture, was designed by Congress to eliminate marketing and trade practices that interfere with the free choice of a producer to join one cooperative over another, or to remain independent and unaffiliated. DFA, in effect, solicits the Secretary's help in eliminating a marketing alternative for members of the Cooperatives.

C. THE DFA PROPOSALS ARE INCONSISTENT WITH UNIFORM PRODUCER PRICE REQUIREMENTS OF THE AMAA.

A significant part of the statutory scheme for promoting orderly marketing is allowing producers of surplus milk and Class I milk alike to share in a uniform blend price, no matter how great the surplus. To achieve this result the act requires:

> ...payment to all producers and associations of producers delivering milk to all handlers of *uniform prices* for all milk so delivered *irrespective of the uses made of such milk* by the individual handler to whom it is delivered.

7 U.S.C. §608(c)(5)(b)(ii)(emphasis supplied). Such sharing of proceeds in the form of uniform producer prices is "the foundation of the statutory scheme." *Zuber v. Allen,* 396 U.S. 168, 179 (1969). Courts, when asked to examine provisions that discriminated between producers, have emphasized the primary objective of price uniformity is "[t]he core of the Congressional program." *Blair v. Freeman,* 370 F.2nd 229, 237 (D.C. Cir. 1966); *see also, Block v. Community Nutrition Institute,* 467 U.S. 340, 341-42 (1984)(a primary purpose of the AMAA is "to assure that the benefits and burdens of the milk market are fairly and proportionately shared by all dairy farmers.").

Advocates of the DFA rule may observe that the PPD would not be directly affected if its proposal is adopted. The rule condemned in *Zuber v.*

Allen violated the Act's uniform price requirement because it discriminated against distant producers in favor of nearby producers in the distribution of pool revenues. However, we do not believe that the mandate of uniform producer prices may be thwarted by a deliberate attack against its flank – in this case, a discriminatory transportation burden imposed on distant producers by government mandate rather than by the producer's free marketing choices.

When Congress considered milk marketing orders and marketwide service payment authority in the 1985 Farm Bill – the Food Security Act of 1985 – the supporting Committee Report expressly recognized that producers who incur disproportionately large transportation costs to supply the fluid needs of the market results in those producers "not receiving uniform prices." H.R. Rep. No. 271, Part I, 99th Cong., 1st Sess. 24-25 (1985), *reprinted in* 1985 U.S. Code Cong. & Admin. News 1103, *et seq.* DFA has come to essentially the same conclusion in its reasoning that the transportation costs associated with its proposal results in an effective reduction of the PPD directly related to extra transportation costs. Hollon, Tr. 395-405. Such non-uniform prices resulting from a regulatory transportation mandate, especially one targeting specific groups of distant producers as proposed by DFA, must clearly be trumped by the superior mandate of the AMAA for "uniform prices" to producers under milk order rules.

D. THE DFA PROPOSALS ARE INCONSISTENT WITH THE ACT'S PROHIBITION AGAINST CONSIDERATION OF A HANDLER'S USE OF MILK AS A CONDITION OF BLEND PRICE RECEIPT.

As quoted above, producer price uniformity is linked to a second, equally important, statutory requirement. The producer is entitled to the uniform price "*irrespective of the uses made of such milk* by the individual handler to whom it is delivered." 7 U.S.C. §608(c)(5)(b)(ii). That is, a price "that did not turn on or vary with the nature of the use for which a producer was able to dispose of his milk...[and that] would not distinguish between producers on the basis of the use made of their milk." *Blair v. Freeman, supra.* The rule at issue in *Blair* was similar to the *Zuber* rule, and provided a bit of extra income from the pool to producers who regularly supplied the fluid (Class I) market.

On this statutory issue, proposals 5 and 7 by DFA are facially vulnerable. These proposals would condition producer eligibility to receive a Central Order blend price (PPD) on the producers' delivery of milk to a Class I distributing plant. Heretofore, all producers could associate with the market by delivery to any pool plant, which may or may not have Class I use; and local (non-distant) producers would still be able to do so under DFA's proposal. As in *Blair,* this

type of provision is unlawful because it conditions blend price eligibility on the use a handler may make of milk.[4]

E. THE DFA PROPOSALS ARE INCONSISTENT WITH THE ACT'S TRADE BARRIER RESTRICTIONS.

The DFA proposals are designed to create a virtually insuperable barrier, in the form of government mandated transportation costs, to participation in the market pool by distant farm milk. This aspect of the proposal also requires a careful examination of 7 U.S.C. § 608(c)(5)(G), as authoritatively construed in *Lehigh Valley Coop. v. United States*, 370 U.S. 76 (1962). Quoting this section, the court in *Polar Co. v. Andrews*, 375 U.S. 361, 379 (1964), noted:

> ...under the present Act authorizing federal marketing orders in the milk industry, such an order may not "prohibit or in any manner limit, in the case of the products of milk, the marketing . . . of any milk or product thereof produced in any production area in the United States." This provision, as the Court explained in Lehigh Valley Coop. v. United States ... was intended to prevent the Secretary of Agriculture from setting up trade barriers to the importation of milk from other production areas in the United States.

Prohibited trade barriers are not in any way limited to the type of pricing provision at issue in *Lehigh.* The provision is broad. As construed by *Lehigh,* it clearly prohibits the type of barrier to distant milk proposed here, which DFA

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[4] The Act allows disparate treatment of handlers on the basis of milk use, as reflected in classified pricing. Thus, it may not run afoul of the Act for the Secretary, as he has long done, to condition a handler's pool plant status on direct or indirect delivery of milk for Class I use. DFA's defense of the proposed requirement on distant producer milk, in that it simply requires a group of outside *producers* to serve the Class I market as if they were a supply plant *handler*, misses the point of § 608(c)(5)(B)(ii), as construed by *Blair.*

itself characterizes as detrimental to outside milk, and would create hardship if imposed on local milk supplies.

F. THE DFA PROPOSAL IS INCONSISTENT WITH EQUAL PROTECTION GUARANTEES OF THE FEDERAL CONSTITUTION.

Government action, including rulemaking, which benefits or burdens affected persons in a disparate manner must pass muster under Equal Protection requirements of the U.S. Constitution. That is, there must be a "rational relationship between the disparity of treatment and some legitimate government purpose." *Heller v. Doe by Doe,* __ U.S. __, 113 S.Ct. 2637, 2642 (1993); *Roper v. Evans*, __ U.S. __, 116 S.Ct. 1620, 1627 (1996). While this is a deferential standard, the economic burdens of a legitimate government purpose may not be disproportionately imposed on one group over another. *Metropolitan Life Ins.Co. v. Ward,* 470 U.S. 869 (1985)(government purpose of promoting the economic welfare of a local industry violated Equal Protection when the means used was to create an discriminatory economic obstacle for outside competitors.); *Tovar v. U.S. Postal Service*, 3 F.3d 1271 (9th Cir. 1993).

We urge the Secretary, therefore, to examine not only the authority under the AMAA for the type of discriminatory rules advanced by DFA, but also to make a critical examination of the purported government interest served by such discrimination and of the reasonableness of such discrimination in

achieving that government interest. On close examination, we believe the Secretary will find that the proposed DFA rule fails even the deferential Equal Protection standard.

CONCLUSION

For the foregoing reasons, the Secretary should terminate this proceeding as to Proposals 1, 3, 5, and 7, or deny the proposals on their merits. For reasons stated in testimony of the Cooperative proponents, proposal 9, which was not substantively opposed, should be adopted.

Respectfully submitted,

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